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No. 83

In the
Supreme Court of the United States
October Term 1948

COMMISSIONER OF INTERNAL REVENUE, PETITIONER,

v.

MARGARET R. PHIPPS, RESPONDENT

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF OF MARGARET R. PHIPPS, Respondent, IN OPPOSITION

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The respondent, Margaret R. Phipps, under authority of Rule 38 of this Honorable Court, files this her brief in opposition to the petition of the Commissioner of Internal Revenue for writ of certiorari to review the judgment of the Circuit Court of Appeals for the Tenth Circuit entered in this case.

OPINIONS BELOW

The opinion of the Tax Court (R. 13-23) is reported at 8 T. C. 190, and the opinion of the Circuit Court of Appeals (R. 30-37) is reported at 167 Fed. (2d) 117.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on March 10, 1948 (R. 38). The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

This case involves a liquidation by a parent corporation of five wholly-owned subsidiaries, four of which had deficits in their earnings and profits accounts, and one of which had a surplus, as of the date of liquidation. The question is whether, on the one hand, the earnings and profits accounts of all five liquidated subsidiaries should be combined in the parent's earnings and profits account, or whether, on the other hand, the surplus of one subsidiary should be included, but the deficits of the other four should be excluded, in determining the earnings and profits of the parent after such liquidation.

STATUTES AND REGULATIONS INVOLVED

The pertinent statutes and regulations are printed in the Appendix to Petitioner's Brief, pp. 16-18.

STATEMENT

In 1937, the Respondent received cash distributions from the Nevada-California Electric Corporation upon stock owned by her, in the total amount of $18,480.00, of which $8,992.28 was paid out of current earnings for the year 1937. This payment, together with corresponding payments to other stockholders, absorbed the entire earnings and profits for the year 1937. The question is whether or not the remainder of $9,487.72, which was not paid out of current earnings, was a taxable dividend. (R. 11)

On December 1, 1936, the Nevada-California Electric Corporation completely liquidated five wholly-owned subsidiary corporations, the liquidations being ones upon which no gain or loss was recognized under I. R. C. Section

112(b)(6). On such date the subsidiaries had earnings and profits accumulated since February 28, 1913, as follows (R. 11-12):

	ACCUMULATED EARNINGS AND PROFITS	
	(Deficit)	(Surplus)
Cain Irrigation Co.	1,740,592.54	
Hillside Water Co.	246,575.75	
The Southern Sierras Power Co.	1,094,697.86	
Yuma Utilities Co.	65,937.47	
The Nevada-California Power Co.		90,362.77

As of December 31, 1936, the parent company had accumulated earnings and profits (since February 28, 1913) in the amount of $2,129,957.81 computed without regard to the accumulated earnings and profits (whether surplus or deficit) of the liquidated subsidiaries, without regard to gain or loss to the parent upon such liquidations, and without regard to prior operating profits or losses of such subsidiaries (R. 12).

If as a result of the tax-free liquidation of the five above listed subsidiaries the accumulated earnings and profits of the parent as of December 31, 1936, cannot be reduced by the amount of the deficits of the other four subsidiaries, then the parent would have a surplus at the beginning of 1937 available for payment of dividends and the sum of $9,487.72 paid to respondent (and similar payments to other stockholders) would constitute a taxable dividend. This is the contention of the Commissioner, the Petitioner herein.

But if the earnings and profits accounts of the parent and the five liquidated subsidiaries must be combined in that account of the parent, i.e., the surplus of the one subsidiary credited and the deficits of the four charged to the parent's accumulated earnings and profits account, then on December 31, 1936, the parent company would not have any surplus in accumulated earnings and profits, but would have a deficit. If this be so, then the sum of $9,487.72 paid to respondent was paid neither out of current earnings for 1937 nor out of accumulated earnings and hence was not a taxable

dividend, but was a payment out of the corporation's capital. This is the contention of the taxpayer, the respondent herein, and the Tax Court (R. 23) and the Circuit Court of Appeals (R. 32) so held.

SPECIFICATION OF ERROR

The respondent contends that no error was committed by the Circuit Court of Appeals in affirming the decision of the Tax Court and in holding that in the case of the liquidation of five wholly-owned subsidiaries under section 112(b)(6) of the Internal Revenue Code, the earnings and profits of the liquidated companies, whether consisting of credit balances or deficits, should be reflected in the earnings and profits account of the parent company and should be taken into account in determining whether distributions subsequently made to stockholders by the parent company were paid out of earnings and profits or out of capital.

REASONS FOR DENYING THE WRIT

1. There is no existing conflict between decisions of Circuit Courts of Appeals for different circuits. The decision of the Circuit Court of Appeals in the case at bar is in harmony with the decisions of the Circuit Court of Appeals for the Second Circuit in *Commissioner v. Sansome*, 60 Fed. (2d) 931, certiorari denied, 287 U. S. 667, and *Harter v. Helvering*, 79 Fed. (2d) 12, and decisions of other Circuit Courts of Appeal since those were rendered; and is not in conflict with the decision of the Circuit Court of Appeals for the Ninth Circuit in *Cranson v. United States*, 146 Fed. (2d) 871, certiorari denied, 326 U. S. 717.

The decision of the Circuit Court of Appeals in the case at bar states the rule of law known as the "Sansome" rule and its application to this case as follows (R. 31-32):

> "In a tax-free reorganization of corporations where a parent liquidates a wholly owned subsidiary, taking over its assets subject to their liabilities in complete cancellation and redemption of its issued and outstanding capital stock, or where two corporations merge, the entire corporate life survives as a continued venture insofar as tax consequences are concerned. A transaction of that kind does not pro-

duce any change in respect of tax purposes, the successor being merely the continuation of the predecessor.

"The principle is not a narrow one, limited to accumulated earnings or profits of the liquidated or absorbed company. It includes a deficit in the earnings or profits account of such company. The earnings and profits accounts of the transferor company, whether consisting of credit balances or deficits, should be reflected in the corresponding accounts of the transferee company and should be taken into account in determining whether distributions subsequently made to stockholders of the emerged company were paid out of earnings or profits or out of capital."

This is the principle enunciated by Judge Learned Hand in the cases of *Commissioner v. Sansome* (1932) *supra*, and *Harter v. Helvering* (1935), *supra*.

In the *Sansome* case, A Company sold out all its assets to B Company, both organized under the laws of New Jersey; the new company assumed all liabilities and issued its stock to the stockholders of A Company. The only change was that the new company's charter gave it broader powers. The latter made no profits and declared a dividend, claimed to be a liquidating dividend, but the court held that since the transaction was non-taxable under Section 202(c)(2) of the Revenue Act of 1921, one of the so-called reorganization provisions of the statute, the identity of the enterprise continued unchanged by the reorganization with the result that the surplus in earnings and profits of the old company remained as surplus in earnings and profits available for dividends. The Court said (p. 933):

"'Hence we hold that a *corporate reorganization which results in no 'gain or loss' . . . does not toll the company's life as continued venture* under section 201 and that what were 'earnings or profits' of the original, or subsidiary, company remain, for purposes of distribution, 'earnings or profits' of the successor, or parent, in liquidation.' (Emphasis ours).

In the *Harter* case there were two separate reorganizations. The first reorganization was a merger of Philadel-

phia Paper Manufacturing Company and Fibre Container Company, each of which had a surplus in its earnings and profits account. The emerging corporation was named New Company. As to this merger, the opinion states (p. 13):

> "When the Philadelphia Paper Manufacturing Company and the Fibre Container Company merged on June 30, 1923, no gain was 'recognized' to the shareholders, for it was a 'reorganization' under section 202(c)(2) of the Revenue Act of 1921 (42 Stat. 229), and section 203(b)(2) of the Revenue Act of 1926, 26 USCA Sec. 934 (b)(2). A consequence of this is that for purposes of allocating dividends under section 201(b) of the Revenue Act of 1926, 26 USCA Sec. 932(b), against earnings before and after March 1, 1913, the surplus is regarded as unchanged. The Commissioner proceeded on the assumption that the shares issued by the New Company, $3,164,750, 'impounded' a corresponding amount of surplus and left for distribution as dividend only the bookkeeping surplus, $1,692,384.34. We have decided otherwise, Commissioner v. Sansome, 60 F. (2d) 931, and the Ninth Circuit agrees. U.S. v. Kauffman, 62 F. (2d) 1045. *Thus the surplus of the New Company was the difference between the assets of both the old companies and the capital shares of both . . .*" (Emphasis ours).

The second reorganization involved in the case was a consolidation of New Company with Boxboard Company. New Company had a substantial surplus in its earnings and profits account but Boxboard had a deficit of $17,388.95. The Court held that upon the merger of New Company and Boxboard Company, the earnings and profits account of the emerging company, which was Boxboard, was not the surplus of New Company undiminished by the deficit of Boxboard Company, but was the contrary, i.e., the surplus of New Company reduced by the deficit of Boxboard Company. Referring to the last sentence in the above quotation from its opinion, the Court expressly pointed out the manner in which this result was reached (p. 13):

> "*Again when in April 1926, the New Company consolidated with the Boxboard Company, the same result ensued, . . .*" (Emphasis ours).

Hence, in the *Harter* case the Court held, as to the first reorganization, that the surplus of the emerging new company was the difference between the assets of both the old companies and the capital shares of both. Then, as to the second reorganization, the Court expressly declared in applying the "Sansome" principle to a merger of a surplus company and a *deficit* company, *the same result ensued* as in the case of merger of surplus companies, to-wit: the successor or emerging company has assets consisting of the total of both companies' assets, and has a surplus or deficit in its earnings and profits account determined by subtracting the combined capital from the combined assets.* As a result of this rule, each constituent company's earnings and profits account continues to exist in the corresponding account of the emerging company,—a surplus in the earnings and profits account is not converted into additional capital, nor is a deficit in the earnings and profits account eliminated by a reduction of capital. This is the so-called "Sansome" rule, and it was followed by the Circuit Court of Appeals in the case at bar.

The decision in the *Cranson* case, *supra*, is not at variance with the foregoing, as both the Circuit Court of Appeals (R. 32) and the Tax Court (R. 21) held in the case at bar.

In the *Cranson* case, a parent company (The Honolulu Oil Corporation, Ltd.) liquidated (tax-free) three wholly owned subsidiaries on August 31, 1936, when the subsidiaries had substantial deficits.

The statute involved in the *Cranson* case was the same as in the case at bar—the Revenue Act of 1936. Section 115(a)(b) (Appendix to Petitioner's Brief, 17) of that Act.

---

*The Court's computations are more fully visualized when set forth in table form as follows:

	Net Assets		Capital		Earnings & Profits
New Company (before merger)	$a	minus	$x	equals	$4,307,134.34 (surplus)
Boxboard Company (before merger)	$b	minus	$y	equals	(17,388.95) (deficit)
One Company (Upon merger)	$(a+b)	minus	$(x+y)	equals	$4,289,745.39 (surplus)

provides that corporate distributions shall be considered as paid first from the earnings of the current year, and then from earnings accumulated since February 28, 1913. To the extent that there are net earnings of the current year, the distribution is a taxable dividend, even though there are no accumulated earnings from prior years, or even if there is a deficit in prior years. In the case at bar this was recognized and the taxpayer conceded (R. 11) and the Tax Court found as a fact (R. 14), that the distributions in the year 1937 were taxable to the extent of the earnings of that year. In the case at bar the sole issue is the effect of the subsidiaries' deficits upon *accumulated* earnings and profits. In the *Cranson* case, however, the taxpayer insisted that the deficits of the subsidiaries should be applied to reduce not the *accumulated* earnings prior to 1936, but the *current* earnings of 1936.

The Court said (p. 871):

> "If Honolulu itself had at the beginning of 1936 the same operating deficit, the deficit could not have been deducted."

and later in the opinion (p. 872):

> "The equation of operating deficit for tax purposes is the loss sustained within the taxable year. As to the alternative contention of the appellant here that if the operating deficits do not diminish the earnings, the losses sustained in the liquidation would diminish earnings, there has been no showing that any of the loss was incurred in the tax year in question. Furthermore, it is apparent that appellent has not maintained its burden of proof that any of the deficits occurred in the tax year 1936. * * * It is hence not before us to consider whether any such deficits would be deductible from the profits of the parent corporation if they had occurred in the tax year 1936.
>
> "Whether or not the parent company suffered losses in the tax years prior to 1936, if there be corporate earnings or profit in that year the Revenue Act of 1936 provides that distributions to the stockholders in that year are deemed to be from its most recently accumulated earnings or profits for that year, without regard to the fact that they are earned

> in that portion of the year after the distribution was made."

It is obvious, therefore, that the Court and the parties were addressing themselves to the question as to whether the deficits of the subsidiaries were deductible from *current* earnings of the year in which the distributions were made.* That question is not involved in the case at bar and was not passed upon by the Tenth Circuit Court of Appeals in its decision in the case at bar.

Petitioner therefore submits that there is no conflict between the case at bar and the *Cranson* case.

Furthermore, the decision in the case at bar is in harmony not only with the decisions of the Circuit Court of Appeals for the Second Circuit in the *Sansome* and *Haxter* cases, but with other decisions applying the "Sansome" rule in the Fourth, Sixth, and Ninth Circuits. The following cases involved tax-free corporate reorganizations or liquidations within the meaning of the Internal Revenue Code or applicable Revenue Acts:

United States v. Kauffman, (CCA 9th, 1933) 62 Fed. (2d) 1045, 1047:

> "In that case (Sansome) it was held that a reorganization of a corporation, * * * wherein the stock-

* Petitioner states (Pet. Br. P. 6) that the total dividend paid by the parent in 1936 amounted to $937,743, and argues that the distribution in 1936 exceeded the 1936 current earnings of $931,553.32 by $6,189.19, and that, as to the latter amount (i.e., 66/100 of 1% of the distribution), the distribution could have been held a dividend only if the parent's accumulated earnings prior to 1936 were not affected by the subsidiaries' deficits. On the basis of this 66/100 of 1% (which as to Mr. Cranson amounted to $2.97) petitioner argues that the court to that extent rendered a decision in conflict with the case at bar. The figure of $937,743 as the amount of the dividend is not mentioned in the decision of the Circuit Court of Appeals in the *Cranson* case, and petitioner ascertains the amount by reference to the record in the case of *Lorin A. Cranson v. United States of America*, No. 85, October Term, 1944, of this Court, which is not part of the record of the case at bar. Reference to the briefs in Case No. 85 discloses, however, that the entire argument was centered on the question of the right to deduct the deficit of the subsidiaries from the *current* earnings of the parent company for 1936 and no reference was made to the question involved in the case at bar.

holders were not taxable for a gain or loss * * * was not such a change in corporate identity as prevented the new company from being *considered as a continuing venture.* * * *." (Emphasis ours):

Gordon Enterprises, Ltd. v. Commissioner, (CCA 4th, 1942), 126 Fed. (2d) 384, 389:

> "The meat of the Sansome case is found in a statement by Circuit Judge Learned Hand * * * 'Hence, we hold that a corporate reorganization which results in no "gain or loss" * * * does not toll the company's life as continued venture.' * * *"

Reed Drug Co. v. Commissioner, (CCA 6th, 1942), 130 Fed. (2d) 288, 290:

> "Such corporate transactions * * *, do not break the continuity of the corporate life."

Robinette v. Commissioner, (CCA 9th, 1945), 148 Fed. (2d) 513, 516:

> "The earnings and profits of Cole-French Company, in existence when liquidation occurred, did not disappear. Either the subsidiary or the parent company had them. * * * The parent completely took over the subsidiary. There is *complete identity* of the corporations." (Emphasis ours).

The foregoing review of the cases decided by the several Circuit Courts of Appeals including that for the Ninth Circuit in the *Cranson* case, and that of the Tenth Circuit Court of Appeals in the case at bar, shows that they all recognize that the underlying theory of the "Sansome" rule is that of the continuity of the corporate existence, and that such continuity requires the merging of the several individual capital accounts and the several individual earnings and profits accounts of the predecessors and parent, or the constituent companies, whether or not the earnings and profits accounts show surpluses or deficits. There is no conflict among the decisions of these Courts.

2. The decision of the Circuit Court of Appeals in the case at bar does not apply the "Sansome" rule in violation of the reasoning of the decisions of this Court.

Petitioner cites only *Commissioner v. Munter*, 331 U.S. 210, in support of his claim that the Circuit Court of Appeals misapplied the "Sansome" rule. In holding that the "Sansome" rule applied to a complicated transaction, the facts of which are not pertinent in the case at bar, the Court said in that case (p. 213):

> "Relying upon the rule of *Commissioner v. Sansome*, 60 F. (2d) 931, *which, for tax purposes, treats a reorganized corporation as but a continuation of its predecessors*, the Tax Court determined that the new corporation acquired all the earnings and profits of its predecessors in 1928." (Emphasis ours).

And at page 215:

> "Congress has repeatedly expressed its approval of the so-called *Sansome* rule as a correct interpretation of the purpose of the tax laws governing reorganizations."

In the case of *Commissioner v. Wheeler*, 324 U.S. 542 (rehearing denied, 325 U.S. 892), this Court had previously stated the Congressional policy which produced the reorganization provisions of the tax laws, and pointed out that the theory of the "Sansome" rule was "sensible," saying (p. 546):

> "'Congress has determined that in certain types of transaction the economic changes are not definitive enough to be given tax consequences, and has clearly provided that gains and losses on such transactions shall not be recognized for income tax liability but shall be taken account of later. Secs. 112, 113. *It is sensible to carry through the theory in determining the tax effect of such transactions on earnings and profits.* Compare *Commissioner v. Sansome*, 60 F. (2d) 931. * * *'" (Emphasis ours).

The use of corporate reorganizations in the early years of the income tax laws to bring about realizations of losses and gains which were, in a sense, artificially produced and not the natural result of the operation of the business involved, was realized by Congress and it decided to discourage manipulations of this type by requiring the participants to postpone any tax effect (advantageous or otherwise) un-

til some event (such as sale of assets) produced a loss or gain which could be accepted as in the normal course of the business of the entire enterprise.

For that reason Congress said that in such transactions neither loss nor gain should be recognized at the time the transaction occurred, and emphasized the factor of continuity of the business venture by providing that the assets of the liquidating company should be set up on the books of the acquiring company at the same tax basis as appeared on the books of the liquidating company. When the acquiring company sold the assets in the future it would incur the same amount of loss or gain as the liquidating company would have incurred had it retained the assets itself; and that amount of loss or gain would at that time be entered in the earnings and profits account.

But the "Sansome" rule recognizes the fact that the provision made by Congress for accounting for loss or gain on the sale of the assets of the group involved in the business venture as though the inter-corporate transactions had not occurred, made no provision for the disposition of the earnings or losses made or suffered in the management and operation of these assets. The "Sansome" rule preserves consistency in the tax treatment of the entire enterprise in requiring the assets of the liquidating company to go over to the acquiring corporation without tax effect, requiring that the capital go over unchanged, and that earnings and profits (whether surplus or deficit) should go over unchanged.

The words "earnings and profits" refer merely to an account; the word "deficit" refers merely to a minus balance in that account; and the word "surplus" connotes simply a plus balance in such account.* Neither the capital account

* In the *Wheeler* case, *supra*, this Court commented on the meaning of the term "earnings and profits," and pointed out that both losses and gains enter into their computation. It follows that losses may exceed gains and the "earnings and profits" account may show a deficit. The *Hazlet* case, *supra*, and the *Senior* case, *infra*, both applying the "Sansome" rule, show that the term "earnings and profits" refers to an account by that name which may or may not have a credit balance or surplus.

nor the earnings and profits account of a corporation stands for or represents any specific assets or any specific property.

The capital account reflects that portion of a company's total assets which is represented by the funds paid in by contributing stockholders as "capital." For tax purposes a corporation's capital as reflected by its capital account remains constant (except as it is increased by contributions from, or decreased by distributions to, its stockholders). The gains or losses of the corporation do not increase or decrease "capital."

The earnings and profits account reflects the difference between the corporation's net assets (i.e. assets minus liabilities) and its capital. Thus the earnings and profits account of a corporation is the balancing figure in an equation. The equation is: net assets (i.e. assets reduced by liabilities) equals capital plus earnings and profits. A company's net assets must always be exactly equal to its capital plus its earnings and profits. This is of necessity so because "capital" and "earnings and profits" are merely tax and accounting expressions used to show how much of total net assets is represented by capital contributed and how much is represented by earnings and profits accumulated.

A corporation which has sustained operating losses sufficiently great so that its net assets are less than its capital, thus has a deficit in earnings and profits. Such a corporation does not have any accumulated earnings and profits out of which dividends can be paid until it realizes sufficient earnings to restore such deficit.*

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* "MEANING OF "ACCUMULATED EARNINGS OR PROFITS." The statute includes in the term 'dividend' not only distributions out of current earnings or profits, but also distributions out of 'accumulated' earnings or profits (since February 28, 1913). Accordingly, prior to the 1936 Act, any distribution, and since the 1936 Act, the excess of distribution over current earnings, is a taxable dividend only if there exist earnings or profits accumulated after February 28, 1913 . . . *An impairment of fixed or statutory capital occasioned by a deficit must be restored out of subsequent earnings before there can be accumulated earnings or profits available for dividends. The same rule governs impairments of capital surplus or paid-in surplus.*" (Emphasis ours). Mertens, Law of Federal Income Taxation, Vol. 1, Sec. 9.30, p. 461.

Eliminating the deficits in computing for tax purposes the earnings and profits account of the successor would mean that for tax purposes the capital investment in the entire venture is reduced by the amount of the deficit eliminated. Four of the five liquidated subsidiaries in the case at bar had substantial operating deficits. Had those subsidiaries not been liquidated but continued as separate corporations, each of them would have been permitted under the tax laws to earn and retain sufficient profits to eliminate the respective deficits. The effect of the lower court's decision is simply that the tax-free liquidation does not reduce the capital, which tax-wise is regarded as invested in such companies before the reorganization, or alter or change the aggregate balance in the earnings and profits accounts of the constituent companies. Upon a tax-free liquidation or reorganization, the entire corporate venture must be viewed as a whole and as so viewed, the combined assets of such venture must represent capital to the extent of the capital that existed before the tax-free transaction and will represent a surplus of accumulated earnings and profits only if such assets exceed such capital.

This was the holding of the court below and, when viewed in the light of the foregoing discussion of the meaning and effect of the "Sansome" rule, the decision is in harmony with the rationale of the decisions of this Court in the *Munter* and *Wheeler* cases.

3. Since the underlying principle of the "Sansome" rule has been settled by decisions of the several Circuit Courts of Appeals which are not in conflict with one another and which are in harmony with the decisions of this court, review by this Court is unnecessary.

The principle of the "Sansome" rule has been recognized by this Court in *Commissioner v. Munter*, *supra*, and *Commissioner v. Wheeler*, *supra*, and adopted by many of the Circuit Courts of Appeals and the Tax Court, as shown in the preceding sections of this brief. Until the case at bar was brought, we have found no record of the refusal of the Commissioner to apply the "Sansome" rule to a deficit case. On the contrary, the Commissioner acquiesced in its applica-

tion in the case of *Senior Investment Corporation v. Commissioner* (1943), 2 T. C. 124, involving a tax-free split-off reorganization. There the Commissioner agreed before the Tax Court that the deficit of a predecessor company should be allocated in a reorganization proceeding and only contended that the amount allocable to the successor corporation was insufficient.

In that case the Tax Court said (p. 137):

> "It is the rule that, where the assets of one corporation pass to a successor corporation in a tax-free reorganization, the accumulated earnings and profits of the old corporation pass to the successor *with the same status* and are available for the payment of dividends by the latter, Commissioner v. Sansome, 60 Fed. (2d) 931; certiorari denied 287 U. S. 667; United States v. Kauffman, 68 Fed. (2d) 1045; Reed Drug Co. v. Commissioner, 130 Fed. (2d) 288; Helen V. Crocker, 29 B.T.A. 773; and that where only part of the assets are so transferred, it is proper to make an allocation of the earnings and profits between the two corporations in proportion to the assets transferred and the assets retained.
>
> "The Respondent (Commissioner) questions the Petitioner's claim that it is a deficit corporation; *but he makes no contention that the principles of the foregoing cases do not apply to the inheritance or absorption of a deficit.* * * *" (Emphasis ours).

Petitioner's suggestion that the decision of the Court below may possibly in future instances lead to tax avoidance does not justify the granting of the writ. This Court itself has laid down the rules which would control attempts

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* Cf. *Helen V. Crocker v. Commissioner*, 29 B.T.A. 773, where the Tax Court said:

> "It is also true that it is merely stipulated that the surplus of the three (predecessor corporations) was sufficient to pay the dividends so that it may be that one of them had a deficit. * * * But we do not think that such a fact, even if true, makes any difference. If the *successor corporation had a surplus inherited from all its predecessors sufficient to pay the dividends, it matters not in what proportions it was contributed.* Such is the effect of our decision in *George F. Baker, Jr., Executor*, 28 B.T.A. 704." (Emphasis ours).

to evade taxes. The purchase of a deficit corporation by a corporation having a surplus for the purpose of liquidating it and offsetting the deficit against the surplus would be defeated by the "business purpose" requirements of such cases as—

Gregory v. Helvering, 293 U. S. 465.
Bazley v. Commissioner, 331 U. S. 737.
Helvering v. Elkhorn Coal Co. (C.C.A. 4) 95 Fed. (2d) 732, certiorari denied, 305 U. S. 605, 670.

In the case at bar there is no suggestion that the motive for liquidation was to avoid taxes, or that the subsidiary companies were acquired for that purpose, or that there was anything except a sound business purpose for the liquidation of the five subsidiaries.

CONCLUSION

For the foregoing reasons it is respectfully submitted that the petition for a writ of certiorari should be denied.

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